



IT IS HEREBY ADJUDGED and DECREED that the below described is SO ORDERED.

Dated: December 16, 2004

A handwritten signature in black ink, appearing to read "R. E. Nugent", is written over a horizontal line.

**ROBERT E. NUGENT
UNITED STATES BANKRUPTCY JUDGE**

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF KANSAS**

IN RE:

**LEWIS EUGENE SEMMEL
JUDY ANN SEMMEL,**

Debtors.

)
)
)
)
)
)
)

**Case No. 01-14433
Chapter 7**

**ORDER ON TRUSTEE' MOTION TO RECONSIDER
EXTENT OF EXEMPTION OF SEMMEL TRUST INCOME**

J. Michael Morris, Trustee, filed a timely motion to reconsider¹ this Court's February 27, 2003 Memorandum Opinion and Order determining that Judy Ann Semmel's beneficiary interest in a trust was exempt and that the bankruptcy estate had no interest in same (the "Order").² The Court denied the motion in part, but granted the Trustee an opportunity to conduct an evidentiary hearing regarding the extent

¹ Dkt. 42.

² Dkt. 39.

of the allowed exemption (the “Reconsideration Order”).³ After some delay, explained below, the Court conducted an evidentiary hearing on October 19, 2004 and is now ready to rule.

Briefly summarized, the pertinent facts here are as follows.⁴ In 1974, Judy Semmel’s aunt and uncle, Bertha and C.C. Ware made a will in which they devised to the First National Bank of Dighton certain real estate in trust for Judy. Under the terms of the trust, Judy was to receive the income from this real estate for life. At her death, the income would be distributed to her children in equal shares until they turned 21, at which time they would receive fee title to the property. When Bertha died in 1985, the Dighton bank declined to serve and Security State Bank was appointed trustee of the trust.

Lewis and Judy Semmel filed their petition in bankruptcy on September 13, 2001. With their petition, they filed Schedule C in which Judy claimed as exempt her interest in the trust. She based this exemption on the provisions of KAN. STAT. ANN. § 60-2310, the wage garnishment exemption statute. Her interest in the trust was described as:

Judy Ann Ware Semmel Trust consisting of continuous income from Real Estate for the period of Judy Semmel’s natural life to be distributed quarterly to the beneficiary.

She valued the exemption at \$10,000 but described the value as an “Estimate Only.” The Trustee in Bankruptcy did not file a timely objection to this exemption. Later, however, he sought to reopen the case to administer newly-discovered assets in the form of the trust and filed a motion to determine the estate’s interest in it.

In its Order, this Court reached two legal conclusions. First, it determined that the trust was not

³ Dkt. 49.

⁴ In the Order, the Court made extensive findings of fact concerning the will and its terms. *See* Dkt. 39.

a spendthrift trust that would be excluded from the bankruptcy estate by virtue of 11 U.S.C. § 541(c)(2).⁵ Second, the Court concluded that by virtue of the Trustee's failure to make a timely objection to the exemption of the trust income, the asset was exempt notwithstanding that the income from the trust is not properly exempt under KAN. STAT. ANN. § 60-2310. The Court concluded, and still believes, that the Supreme Court's decision in *Taylor v. Freeland & Kronz* mandates that conclusion.⁶

It is this Court's holding that the entirety of Judy Semmel's trust interest was exempt that the Trustee asks to be reconsidered. He filed a timely motion for reconsideration which, after a hearing, the Court granted in part and denied in part.⁷ In its Reconsideration Order entered on May 10, 2003, this Court granted the motion to reconsider the extent of the exemption by ordering that an evidentiary hearing on the degree and extent of the exemption be conducted. Debtors then appealed the Reconsideration Order to the Bankruptcy Appellate Panel⁸ which subsequently dismissed the appeal after finding that the Reconsideration Order was interlocutory. The BAP mandate was entered on this Court's docket on June 26, 2003.⁹

Thereafter, the parties attempted to conduct discovery, but were thwarted, at least to a degree, by

⁵ Dkt. 39, Order, p. 6.

⁶ 503 U.S. 638, 112 S.Ct. 1644, 118 L.Ed. 2d 280 (1992).

⁷ Dkt. 49. The Court notes that in the briefs presented prior to the Order, neither party raised or alluded to ambiguity of the debtor's claim of exemption. Both briefs concentrated on whether or not the trust was a spendthrift instrument. Notwithstanding that, because the Court believes it may have misperceived the law respecting the scope of *Taylor* exemptions, reconsideration is appropriate here.

⁸ Dkt. 51.

⁹ Dkt. 64.

Judy Semmel's deteriorating health. The Trustee was apparently never able to preserve her testimony, although he did obtain discovery from the Bank. This Court continued the evidentiary setting several times to accommodate Ms. Semmel's health and medical concerns. Unfortunately, she succumbed to her illness, dying on October 13, 2003. A suggestion of death was filed on April 19, 2004.¹⁰

At the evidentiary hearing, the parties stipulated to the admission of several exhibits which included debtors' Schedule C, a July 6, 2001 letter from Tommy Beaton at Security State Bank to Ms. Semmel, and a summary of the income and expenses of the Judy Ware Semmel Trust from the petition date until the date of Ms. Semmel's death. This exhibit also contained a statement of income and expenses for the trust from Ms. Semmel's death through July 20, 2004. That exhibit states that from September 2001 through October 13, 2003, the trust realized income of \$33,358.40 and incurred expenses of \$10,138.76, yielding net income of \$23,219.64. Ms. Semmel received a distribution of \$10,920 after the entry of the February 27, 2003 Order and the Trustee announced at the hearing that he lays no claim to these funds. Rather, he seeks the remaining \$12,299.94 net cash and may also seek \$5,180.96 in net cash accumulated the year after Ms. Semmel's death.

The Beaton letter is notable in that it contains a summary of the trust's economic activity for 1999 and 2000. Ms. Semmel's 2000 trust income was \$6,600. Her 1999 income was \$11,400. On the fax cover sheet is a notation, dated August 27, 2001: "Per Mr. Beaton Judy's Income should be in the 10,000 to 12,000 [sic] range for 2001"¹¹ The trustee apparently relies on this statement, in concert with the

¹⁰ Dkt. 78.

¹¹ Ex. 4. This notation, on a fax cover sheet addressed to Ms. Roberts, Ms. Semmel's counsel, was likely made by Ms. Roberts, perhaps after a phone call with Mr. Beaton.

\$10,000 “estimate” given on Schedule C, to support his contention that Ms. Semmel intended to exempt only that year’s income. Of course, the Schedule C reference also claims “continuous income from Real Estate for the period of Judy Semmel’s natural life” Seeking to exempt “continuous income” and “estimating” the value of that income at \$10,000 are inconsistent. Finally, Ms. Semmel’s counsel stated at the hearing that she believed Ms. Semmel intended to exempt one year’s income, but this apparent concession is not evidence. Even treating counsel’s statement as evidence, the record before the Court as to the intended result of the purported exemption is ambiguous at best.

In the years since *Taylor*, several bankruptcy courts have attempted to define the parameters of exemptions improperly claimed, but not objected to by bankruptcy trustees. In general, the trend has been to limit the extent of these exemptions to the amounts or extent referenced by the debtors in their schedules. In *Taylor*, the debtors attempted to claim as exempt the proceeds of a lawsuit for wrongful termination and back pay, invoking 11 U.S.C. § 522(d)(11) which allows an exemption of, among other things, payments on account of wrongful death or pain and suffering. The debtor there did not specify an amount claimed exempt but thereafter sought to retain an award of some \$110,000 after the trustee failed to object, even though under either state or federal exemption law, debtor’s exemption would have been considerably less. The Supreme Court held that the exemption objection deadline is a firm one and that 11 U.S.C. § 522(l) is to be interpreted literally as a clear and unambiguous deadline to be met by the trustee. If an exemption objection is not timely filed, the exemption will stand whether or not it would have survived a timely filed objection.

The courts that limit the scope of *Taylor* base their reasoning on the perceived ambiguity of the debtor’s claim of exemption. For instance, in *In re Clark*, the Ninth Circuit Bankruptcy Appellate Panel

concluded that because the debtor controls the content of the schedules, any ambiguities contained in them will be construed against the debtor and in favor of the creditors.¹² Where the exemption claim is so ambiguous as to not place the trustee on notice of what is being claimed, the trustee's failure to make a timely objection does not result in an automatic exemption. There, the debtor claimed five lots which he asserted were held in a retirement plan when, in fact, the lots were owned by him. The trustee did not make a timely exemption objection, but when he discovered the true title to the lots, sought to sell them in a 11 U.S.C. § 363 sale. The BAP affirmed the bankruptcy court's order overruling the debtor's sale objection.

A case more similar to ours is *In re Hurdle*, where the debtors sought to exempt royalties by scheduling them on Schedules B and C as having values of \$807 and claiming them exempt under the California wage and earnings exemption statute.¹³ Believing they were only exempting \$807, the trustee made no timely exemption. Debtors then asserted they were entitled to the entirety of the stream of royalties, not just the \$807. The bankruptcy court considered whether the schedules placed the trustee on sufficient notice of the debtors intentions so that he could determine whether or not to object and concluded that by giving a dollar value to the exemption claimed, the debtors gave no notice that their claim went beyond that amount.

Another court has held that when a debtor claims an exemption based upon a statute with a dollar limit, even though the debtor states the value is "unknown," the exemption is limited to the statutory amount. In *In re Wick*, the debtor scheduled certain stock options and valued them as "unknown," but cited to the

¹² 266 B.R.163 (9th Cir. BAP 2001), citing *In re Hyman*, 967 F.2d 1316 (9th Cir. 1992).

¹³ 240 B.R.617 (Bankr. C.D. Cal. 1999).

federal “wildcard” exemption provided in 11 U.S.C. § 522(d)(5) that has a dollar limit.¹⁴ Even though the trustee did not object, the court held that the trustee was entitled to all of the asset’s value above the wildcard limit, again because the exemption claim was ambiguous.

Here, the claim is less than clear, but only somewhat ambiguous. On the Statement of Financial Affairs, Ms. Semmel disclosed income from the trust over a period of several years. The interest is described there as “Judy Ware Semmel - Trust.” On Schedule B, the trust is disclosed as a contingent and non-contingent interest and described as:

Judy Ann Ware Semmel Trust consisting of continuous income from Real Estate for the period of Judy Semmel’s natural life to be distributed quarterly to the beneficiary.

The asset is valued at “\$10,000 - estimate only.” On Schedule C, the asset is claimed exempt and its description is identical to that on Schedule B. The exemption is claimed under the Kansas wage exemption statute, KAN. STAT. ANN. § 60-2310 which is, of course, inapplicable. As the Court noted in its Order, this is a potentially frivolous exemption claim as there is no authority of which this Court is aware that would bring trust income under the definition of “earnings,” the asset which § 60-2310 operates to protect.¹⁵ However, even after the October 19 evidentiary hearing, the record still lacks any evidence of Ms. Semmel’s intent in electing this exemption. This Court cannot conclude on this sparse record that the claimed exemption violated Fed. R. Bankr. P. 9011.

The Court is also perplexed at how the Trustee can claim to have been “misled” here. In no fewer

¹⁴ 276 F.3d 412 (8th Cir. 2002).

¹⁵ “Earnings” are defined as “compensation paid or payable for personal services . . .,” *see* KAN. STAT. ANN. § 60-2310(a)(1).

than four places¹⁶ in the initial filing, the petition describes this income as coming from the Judy Ann Ware Semmel Trust. And, in Schedules B, C and I, the income is specifically described as coming from real estate, thus making it very clear to even a casual reader that the income stream is not “earnings” within the meaning of § 60-2310(a)(1). The Trustee offered no evidence concerning his initial analysis of this exemption claim or what caused him to demand the Bank turn over the income, but the fact that he made the demand suggests that, at some point in time, he became aware that this asset was not “earnings” per se.

Had the Trustee harbored doubt about the true nature of the trust income, he could have sought (and would likely have received) an extension of the Fed. R. Bankr. P. 4003(b) time in which to lodge an objection. He did not do that. Instead, he now relies on the judge-made “ambiguity exception” to *Taylor* and 11 U.S.C. § 522(l). The only ambiguity this Court sees in the exemption claim arises out of its estimated value of \$10,000. That indeed appears to have been an accurate estimate of the prepetition income for 2001. Ms. Semmel did receive \$10,920 in distributions for that year. It seems unlikely that the Trustee would have *declined* to object to a \$10,000 exemption item and it is difficult to see how he was even misled by this statement. Nevertheless, the weight of persuasive authority seems to be that *Taylor* exemptions may be limited by the express language in which they are couched.¹⁷ The trust income exemption in this case is very similar to the royalty exemption in *Hurdle*. In both cases, the exemption is described as an expectation of a stream of income and, in both cases, only one period’s worth of the

¹⁶ The trust is also identified as a source of income on Schedule I.

¹⁷ See William L. Norton, Jr., 2 NORTON BANKRUPTCY LAW AND PRACTICE 2D, § 46:33, pp. 46-104-106 (2004) and cases cited therein; Lawrence P. King, 4 COLLIER ON BANKRUPTCY ¶ 522.05[2][b] (15th Ed. Rev. 2004).

stream is noted as the estimated value. In *Hurdle*, the court construed the ambiguously scheduled exemption against the debtors and concluded that they could only exempt one month's royalties, or \$807.¹⁸

Although this Court has some doubt about the ambiguity present here, a similar result is in order. During the course of the case, Ms. Semmel received \$10,920, apparently with the Trustee's concurrence. This amount shall be deemed exempt from the Trustee's reach.¹⁹ Absent a valid exemption, the estate succeeds to the debtor's property interests on the date of the petition, as well as any profits therefrom.²⁰ Thus, the Trustee is entitled to collect from the Judy Ann Ware Semmel Trust any sums to which Ms. Semmel would have been entitled, less the valid exemption discussed above. As Ms. Semmel's interest was a life estate and the express terms of the trust provide for her children to succeed to her income interest upon her death if they are younger than 21 years of age and to succeed to the real property in fee upon their reaching 21, the bankruptcy estate's income rights expired with Ms. Semmel on October 13, 2003. The net cash accumulated in the Trust, but not distributed, from the date of bankruptcy until the date of Ms. Semmel's death, or \$12,299.64, is property of the estate and should be paid to the Trustee for the benefit of the Semmels' creditors. The net income accruing after October 13, 2003 is, by virtue of the trust terms, the property of Ms. Semmel's children in equal shares. It is not property of the estate.

In closing, the Court notes that this matter has consumed a significant quantity of its resources, as well as those of the parties involved. The Court is particularly troubled that this dispute lasted literally for

¹⁸ 240 B.R. at 624-625.

¹⁹ In his Motion, the Trustee also raises the 75 percent limitation on the Kansas earnings exemption as a possible means of limiting Ms. Semmel's exemption here. For the purpose of this case only, the Court takes the debtor's "estimated" valuation as the net value of the exemption.

²⁰ 11 U.S.C. § 541(a)(1), (a)(6).

the balance of Ms. Semmel's life and that it was, no doubt, a burden to her in her final days. Had a timely objection to the exemption been made, a result more favorable for the estate (and more humane for the debtors) might have been efficiently and promptly reached. As the Ninth Circuit BAP stated in *Clark*:

As this case illustrates, trustees risk costly delays and the uncertainty of litigation and appeals when they assume that failure to object to an imprecise and unsupported exemption claim will not result in automatic exemption under *Taylor*. By far the safer approach would be for trustees to take a conservative and skeptical view of exemption claims, and refuse to accept any claim of exemption that is not clearly legitimate on its face.²¹

Reliance upon the case-law exceptions to *Taylor* after the fact is no substitute for a trustee's timely objection to a questionable exemption.

The Trustee's Motion to Reconsider is GRANTED to the extent that the allowed exemption is limited to the \$10,920 received by Ms. Semmel from the trust on March 5, 2003. The balance of the trust's net income accrued to the date of her death, or \$12,299.64, is not exempt and is property of the estate. Any income of the trust after her death is not property of the estate and the Trustee has no claim thereto. This Court's Order of February 27, 2003 is modified accordingly.

IT IS SO ORDERED.

#

²¹ 266 B.R. at 171.